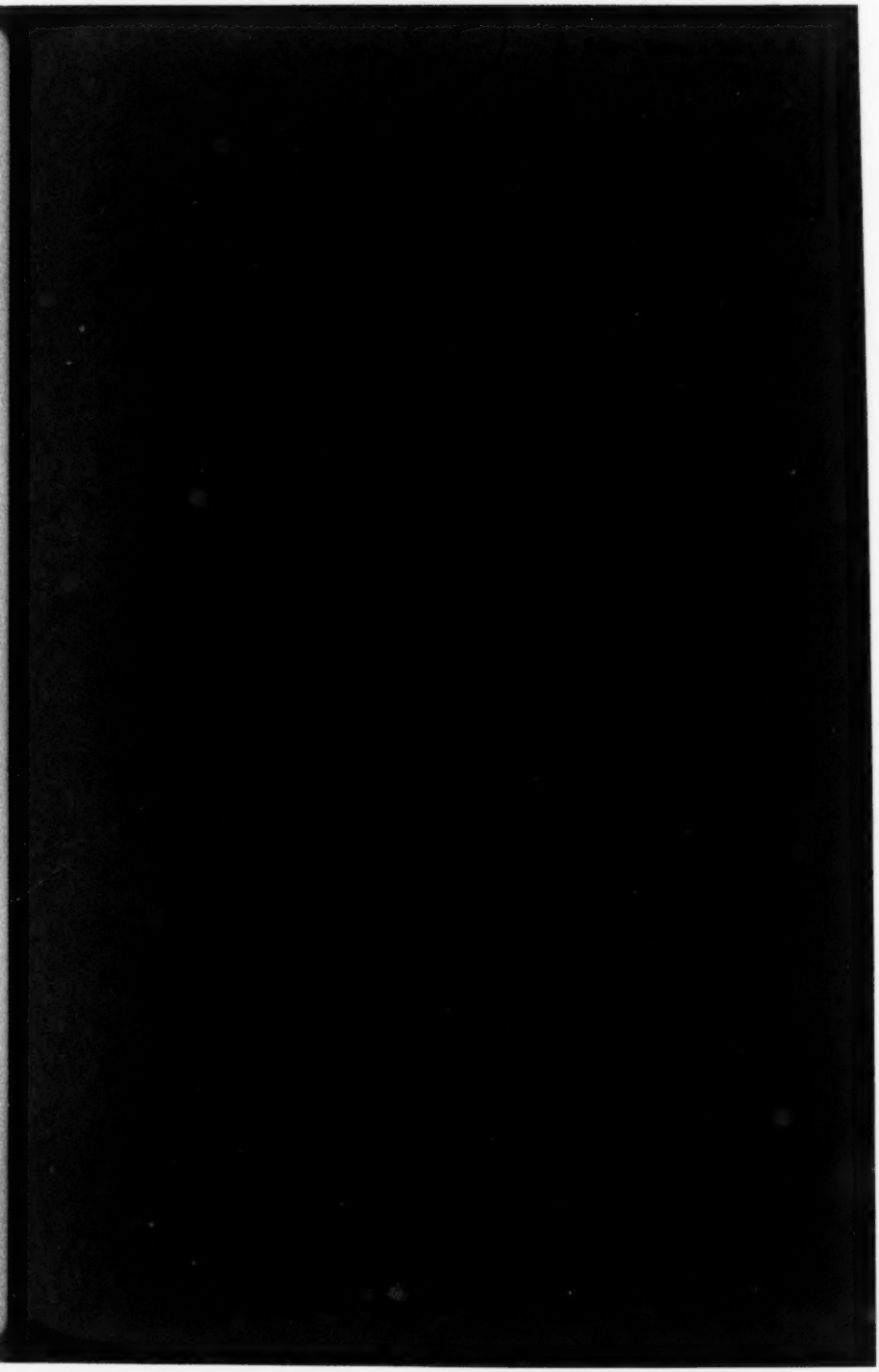

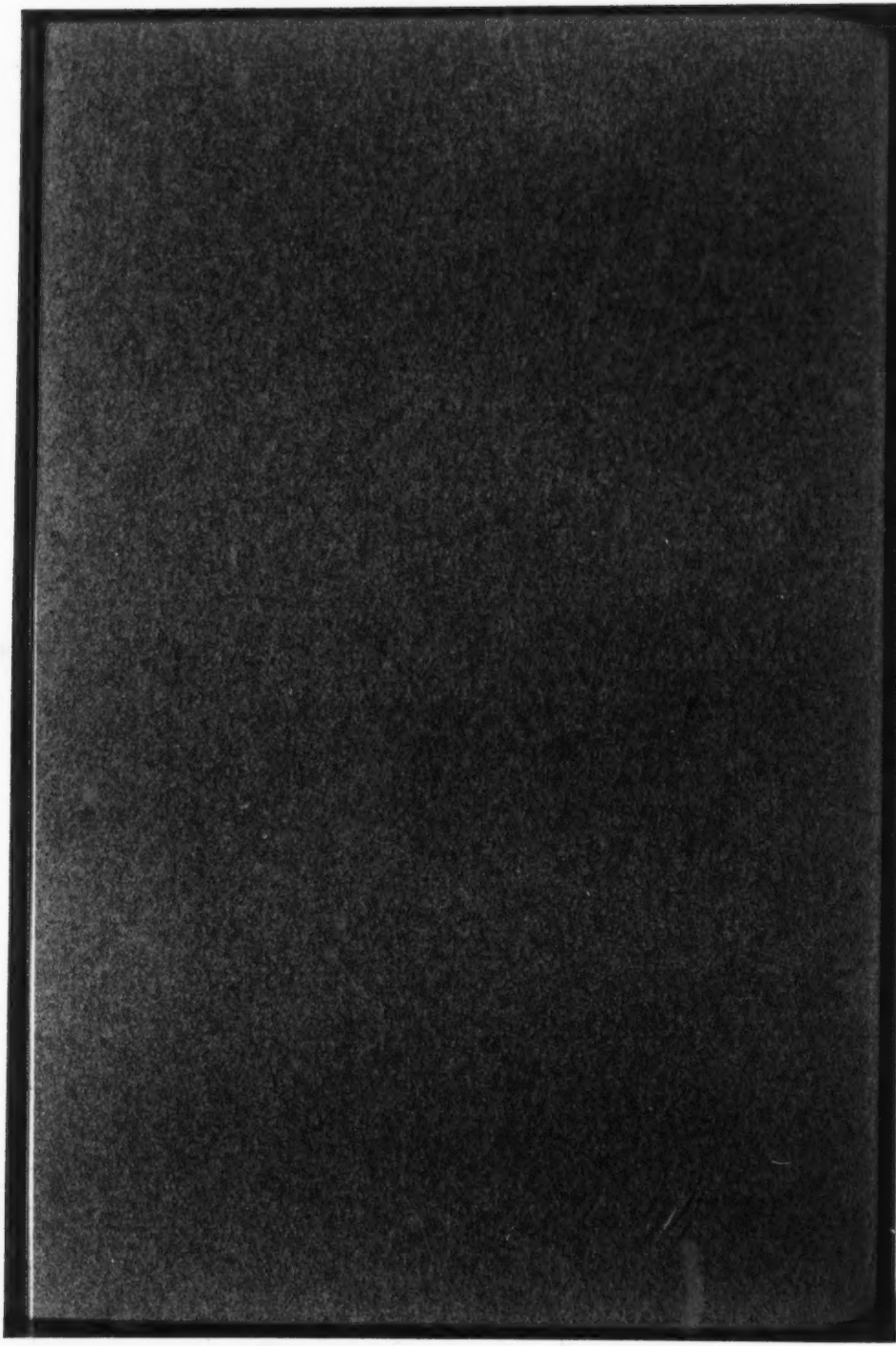

INDEX

CITATIONS

517104—43——1

In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 772

THE NEW YORK TRUST COMPANY, AS THE TRUSTEE UNDER THE DEBENTURE AGREEMENTS BETWEEN IT AND THE UNITED LIGHT AND POWER COMPANY, ET AL., PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION AND THE UNITED LIGHT AND POWER COMPANY

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

OPINIONS BELOW

The findings and opinion of the Commission (R. 294–315), not yet officially reported, are set forth in the Commission's Holding Company Act Release No. 3658. The opinion of the circuit court of appeals (R. 320–325) is reported in 131 F. (2d) 274.

JURISDICTION

The decree of the circuit court of appeals was entered December 4, 1942 (R. 326). The petition for a writ of certiorari was filed February 27, 1943. The jurisdiction of this Court is invoked under Section 240 of the Judicial Code as amended by the Act of February 13, 1925, the provisions of which are made applicable by Section 24 (a) of the Public Utility Holding Company Act of 1935.

QUESTIONS PRESENTED

1. Whether the Commission, after making a valid order directing a registered holding company to dissolve pursuant to Section 11 (b) (2) of the Public Utility Holding Company Act of 1935, has the power pursuant to a plan submitted to it to approve and direct retirement of the company's unmatured debentures upon finding that the retirement is "necessary to effectuate the provisions of said section" and "fair and equitable to the persons affected."

2. Whether the Commission may under such circumstances approve and direct retirement of the debentures at par and accrued interest without payment of the premium specified by the debenture agreement for redemption and without compensation for the termination of the investment.[1]

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[1] The petition for certiorari states other questions which are embraced within those stated, or are too trivial for separate consideration.

STATUTE INVOLVED

The applicable provisions of the Public Utility Holding Company Act of 1935 are set forth in an Appendix, *infra,* pp. 16–22.

STATEMENT

On December 6, 1940, the date of the commencement of the proceeding in which the Commission's order was entered, United Light and Power Company ("Power") was a registered gas and electric utility holding company at the top of a system embracing fifty-two companies, of which seven were registered holding companies (R. 99–100, 111). Power owned directly the securities of a number of its utility operating subsidiaries, but most of the operating companies in the system were controlled through one or more subholding companies.

The proceeding before the Commission was commenced by notice and order for hearing to determine whether it was necessary under Section 11 (b) (2) of the Act to require the simplification of the system of Power and the discontinuance of the existence of one or more companies in the system (R. 3–9). The petitioners here were given notice of the proceeding by publication (R. 8–9). After hearings (R. 10–90) the Commission on March 20, 1941, issued its findings, opinion and order, finding that the liquidation and dissolution of Power was necessary to comply with the requirements of Section 11 (b) (2) and, particu-

nearly with the second sentence thereof, commonly known as the "great-grandfather" provision (R. 91–113).[2] The Commission therefore ordered Power to liquidate and dissolve with due diligence (R. 115–116). The general outlines of a plan of liquidation were described in the Commission's opinion (R. 101–104). No petition to review this order has been filed and the time for review has expired.[3]

Following the entry of the order of liquidation and dissolution, the Commission approved various applications filed by Power with respect to transactions necessary to carry it out (R. 117–131, 135–176).[4] The applications were filed under Sec-

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[2] The second sentence of Section 11 (b) (2) provides as follows: "In carrying out the provisions of this paragraph the Commission shall require each registered holding company (and any company in the same holding-company system with such holding company) to take such action as the Commission shall find necessary in order that such holding company shall cease to be a holding company with respect to each of its subsidiary companies which itself has a subsidiary company which is a holding company."

The effect of this provision is to require that a holding company system be limited to a maximum of three tiers of companies.

[3] Section 24 (a) of the Act provides that a petition for review of an order of the Commission must be filed within sixty days after the entry of the order.

[4] The record references are to the Commission's findings, opinions and orders on Applications Nos. 1 and 5. Orders granting Applications Nos. 2, 3, 4, 6, and 7 are not in the printed transcript but are a part of the transcript of record certified by the Commission.

tion 11 (e) of the Act as steps in the program for compliance with Section 11 (b) (2) and the Commission's order thereunder.

As a step in this process Power, on January 20, 1942, filed with the Commission its Application (No. 8) under Section 11 (e) to liquidate and retire its outstanding debentures at their total principal amount of $15,093,800 plus interest accrued to May 1, 1942 (R. 178–185). These debentures were unsecured obligations of Power, issued in three series in 1923, 1924 and 1925, bearing interest until maturity at coupon rates of 6%, 6½%, and 6% respectively, and due by their terms in 1973, 1974 and 1975, respectively.[5] Under the terms of the debentures and debenture agreements, Power had the "right", "election" and "option" to redeem the debentures in whole or in part before maturity by paying the principal and accrued interest, plus a "premium" in an amount which, at the date of this proceeding, was $9 on each $100 principal amount (R. 222, 226, 229), or, in the aggregate, $1,358,442 on the debentures then outstanding.

[5] The 1923 debentures had been issued by United Light and Railways Company (of Maine), a predecessor of Power, which was afterward dissolved. Power assumed the obligation of these debentures and issued the 1924 series under the same debenture agreement. The 1925 debentures were issued under a separate agreement. The material provisions of both debenture agreements are substantially identical. For the purpose of this case all of the debentures may be treated as if issued under one agreement.

The Commission held hearings on the application. The New York Trust Company, as trustee for each of the debenture series, and certain debenture holders not parties to the review in the court below, intervened and contended that Power was required to pay either the redemption premium of 9% or compensation for the termination of the investment (R. 286–293, 313–314).[6] After briefs and argument (R. 243–285, 297), on February 25, 1942, the Commission issued its Findings, Opinion and Order approving the Application under the standards of Section 11 (e); it found that the retirement of the debentures as proposed by Power was "necessary to effectuate the provisions of said section [11 (b) (2)] and to enable Power to liquidate and dissolve in accordance with our order of March 20, 1941," and that the plan was "'fair and equitable' to the persons affected thereby" (R. 294–318).[7]

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[6] In anticipation of this contention, Power's Application further provided that upon entry of an order approving the plan, Power would give notice of payment to all registered owners of debentures; that an escrow agreement would be executed covering the deposit of cash of Power to provide the payment of debenture premium in the event of a reversal of the Commission's order upon judicial review; and that debenture holders surrendering their debentures for payment would not thereby waive the redemption premium if, upon review, it should be determined that they were entitled thereto (R. 184–185).

[7] On March 4, 1942, Power filed a certificate of notification stating that the transactions described in Application No. 8 had been carried out (R. 319).

On a petition for review, the Circuit Court of Appeals for the Second Circuit affirmed the Commission's order (R. 320–327).

ARGUMENT

The questions presented arise out of a program of corporate simplification required by Section 11 (b) (2) of the Public Utility Holding Company Act of 1935. They and allied questions are recurring and therefore in one sense are important in the administration of the Act. But, it is submitted, there can be no serious doubt of the correctness of the decision upon those issues by the court below; and in *City National Bank & Trust Co.* v. *Securities and Exchange Commission, et al.*, decided March 5, 1943, the Circuit Court of Appeals for the Seventh Circuit has decided the same issues in the same manner.[8] Under these circumstances, there would seem to be no occasion for review by this Court.

1. The Commission plainly had power to determine what disposition should be made of the debentures and to direct that they be retired upon finding, as it did, that such a step was "necessary to effectuate" the provisions of Section 11 (b) (2).

Petitioners' arguments that it was not necessary that the debentures be retired in order to

[8] The opinion is not yet reported but is reprinted in the Appendix, pp. 23–36, *infra*.

comply with Section 11 (b) (2) (Pet. 11–16), that regulation of the debentures was not constitutional under the commerce clause (Pet. 16–17), that such regulation violated the Fifth and Tenth Amendments (Pet. 17–19), and that such regulation violated Section 26 (c) of the Act (Pet. Br. 14–16) are all based on a misunderstanding of the relationship between the order of retirement and the dissolution proceeding in which the order was entered.

The order under attack was entered after an earlier order of the Commission in the same proceeding requiring Power to liquidate and dissolve in order to comply with Section 11 (b) (2) of the Act.[9] No review of this order had been sought and the order was final. Accordingly, the constitutional and statutory warrant for that order are not now open to challenge.

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[9] The Commission's liquidation order was not, as petitioners contend, based solely on the "great-grandfather clause." Indeed, that clause is by its terms merely a specific application of the broader policies of the balance of Section 11 (b) (2).

The Commission's proceeding was directed to the broad question of what action should be taken by Power and its principal subsidiaries "pursuant to Section 11 (b) (2) of said Act requiring the simplification of the corporate structure of the holding company system of The United Light and Power Company and the simplification of the corporate structure and discontinuance of the existence of one or more companies in said holding company system," and of "what steps and what action is necessary for that purpose" (R. 7–8).

Since an order of dissolution obviously does not of its own force accomplish liquidation and dissolution, it is always necessary to develop a plan for accomplishment of the order in accordance with the rights of creditors and stockholders. Accordingly, the Act makes formulation and superintendence of the program for accomplishing liquidation an integral part of the corporate simplification proceeding. Section 11 (d) provides that where the Commission applies to a court to enforce compliance with its simplification order under Section 11 (b), compliance must be accomplished in accordance with a "fair and equitable" plan which shall have been approved by the Commission. Section 11 (e) provides that where, as in the present case, the company comes forward with a program for simplification in compliance with Section 11 (b), then the Commission shall find whether the plan is necessary to effectuate the provisions of subsection (b) and fair and equitable to the persons affected by such plan, and, if it does, shall enter an order approving the plan. Thus, in every case the Commission is required to see that compliance with Section 11 (b) (2) and its orders thereunder is carried out in accordance with a plan which is fair and equitable and in accordance with the rights of the parties. Clearly, therefore, the Act empowers the Commission to determine and adjust the rights of the debenture holders whenever such

an adjustment is an appropriate incident to the corporate simplification. The word "necessary" does not mean absolutely prerequisite; it leaves some scope for discretion.[10] In these provisions the Act carries out the public policy, also expressed in antitrust cases, of protecting the rights of security holders affected by the exercise of paramount public policy exercised under the commerce power (see *United States* v. *American Tobacco Co.*, 221 U. S. 106, 185).

It is plain, therefore, that the Commission acted within the scope of its statutory powers in the instant case. And since petitioners have conceded—and, indeed, cannot here deny—the validity of the Commission's liquidation order, there can be no serious constitutional challenge to the exercise of power to supervise and direct the detailed steps of the liquidation program, including payment of the debentures, as an incident to the effectuation of the Commission's order and the purposes of the Act. The decisions in antitrust cases show decisively that the federal government has the power to exercise such an incidental jurisdiction in order to implement a broad exercise of the commerce power. *Continental Insurance Co.* v. *United States,* 259 U. S. 156; *United States* v. *American Tobacco Co.,* 221 U. S. 106; *Northern Securities Co.* v. *United States,* 193 U. S. 197; *Standard Oil Co.* v. *United States,* 221 U. S. 1.

[10] Cf. *McCulloch* v. *Maryland*, 4 Wheat. 316, 413 *et seq.*

Nor was the action of the Commission unconstitutional because the contract rights of the debenture holders are affected. To show that a reasonable exercise of federal power may result in the termination of antecedent contracts of innocent persons does not establish a denial of due process under the Fifth Amendment or violate the "basic principle underlying the Constitution," as petitioners contend. See *Louisville & Nashville R. R.* v. *Mottley,* 219 U. S. 467, 480–486; *Philadelphia, etc., R. Co.* v. *Schubert,* 224 U. S. 603; *United States* v. *Southern Pacific Co.,* 259 U. S. 214, 234–235; *Norman* v. *Baltimore & Ohio R. Co.,* 294 U. S. 240; cf. *Addyston Pipe & Steel Co.* v. *United States,* 175 U. S. 211. And since the power exercised is granted under the commerce clause, there is no invasion of any rights of the States reserved under the Tenth Amendment. *United States* v. *Darby,* 312 U. S. 100.[11]

As to the merits of the Commission's conclusion that the debentures had to be retired, there

[11] Petitioners' contention that under Section 26 (c) of the Act the Commission may not terminate contract rights anteceding the Act is obviously unsound. That section, and its correlative, Section 26 (b), specify what securities shall be valid or invalid under the Act with reference to the question whether their issuance complied with the regulatory provisions of the Act. Any restrictive reading of Section 26 (c) denying the Commission the power to terminate securities contracts entered into prior to the passage of the Act would prevent the attainment of the specific objectives of Section 11 (b) (2), which are to deal with, and under certain circum-

can be little question. Disposition of the debentures was obviously an essential part of the liquidation. The Commission found that no disposition was possible other than retirement. It considered ~~ation. The Commission found that no disposition~~ other possible dispositions and found that the assumption of the debentures by any other company in the system was not feasible nor proper as a financial matter and in the light of the standards of the Act (R. 299–301). The findings of the Commission on these points may not be disturbed upon review for there is no showing that the Commission abused its discretion. *Gray* v. *Powell*, 314 U. S. 402.

2. The remaining question is whether the Commission erred in finding that the plan providing for immediate repayment of principal and accrued interest was fair and equitable to the debenture holders even though it did not require Power to pay them additional compensation for the premature termination of their investment. As matters stood before institution of the proceeding, the debenture holders had a contract right to receive interest until 1973–1975 and the principal

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stances to require the liquidation of, holding companies existing when the Act was passed, all of which had securities long ago issued and outstanding. In disposing of the debentures the Commission did not declare them to be invalid and not entitled to be recognized in the liquidation, but merely required their retirement on "fair and equitable" terms as an incident to action necessitated by Section 11 (b) (2).

at that time, subject only to the right of the company to redeem the debentures earlier at an agreed premium. The debenture holders contended before the Commission—as do the petitioners here—that they were entitled to be compensated for the loss of that right. The Commission rejected the claim and its decision, we submit, was plainly sound.

The Commission first considered the debenture agreements and found that properly construed they contained no provision for payment of a premium or other compensation in the event of forced prepayment under the compulsion of a statute passed long after the debentures had been issued. The court below agreed. The provision for a premium in the event of voluntary redemption of the debentures at the "option" or "election" of the company (R. 221, 226, 229, 231–232, 242) is obviously unsuited to describe this situation in which Power was compelled to pay off the debentures to comply with the Commission's order of liquidation and dissolution.[12]

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[12] Indeed, the provisions of the debenture agreements, executed in 1923–1925, could not possibly have envisioned the Commissioner's order of liquidation and dissolution under Section 11 (b) (2) of the Public Utility Holding Company Act enacted in 1935. Therefore, even if the language of the debenture agreements read literally might be considered as descriptive of the situation, it would not be construed to apply to these circumstances which were not foreseeable when the language was used. *Chicago, Milwaukee & St. Paul Railway Co.* v. *Hoyt* 149 U. S. 1; *In re Bond & Mortgage Guarantee Co.*, 267 N. Y. 419.

Second, in conformity with general contract law the Commission held that apart from the option provision the debenture holders were not entitled to compensation for the termination of their investment. This determination, which the court below also approved, finds clear support in decisions of this and other courts which uniformly hold that when private contracts entered into prior to the enactment of federal laws are terminated by operation of those laws, neither contracting party is entitled to compensation for breach thereof. *Louisville & Nashville R. R.* v. *Mottley,* 219 U. S. 467; *Lewis, Leonhardt & Co.* v. *Southern Ry. Co.,* 217 Fed. 321 (C. C. A. 6); *Elliott Mach. Co.* v. *Center,* 227 Fed. 124 (W. D. Mich.); *Louisville & N. R. Co.* v. *Crowe,* 156 Ky. 27; *Cowley* v. *Northern Pacific Railway Co.,* 68 Wash. 558.

In terminating the debenture holders' right to retain the investment, the Commission necessarily, at the same time, terminated the correlative right of Power and its stockholders to use the borrowed capital until maturity upon payment of interest for its use. Thus, the whole agreement between Power and its debenture holders was frustrated by operation of law. Under such circumstances the debenture holders were not entitled to compensation. A promisee is not entitled to compensation for the loss of his bargain when the promisor has been denied his expected benefits as a

result of the elimination, under the impact of a domestic law, of an essential factor which both parties assumed would continue—the lawful existence of Power, in the instant case. *Texas Company* v. *Hogarth Shipping Company,* 256 U. S. 619; *Lorillard* v. *Clyde,* 142 N. Y. 456; *Heart* v. *East Tennessee Brewing Co.,* 121 Tenn. 69; *Adler* v. *Miles,* 126 N. Y. Supp. 135 (Sup. Ct. App. T.); *McCullough Realty Co.* v. *Laemmle Film Service,* 181 Ia. 594; *Industrial Development & Land Co.* v. *Goldschmidt,* 56 Cal. App. 507; *Doherty* v. *Monroe Eckstein Brewing Co.,* 187 N. Y. Supp. 633 (Sup. Ct. App. T.); *Wischhusen* v. *American Medicinal Spirits Co.,* 163 Md. 565; *King Features Syndicate, Inc.* v. *Valley Broadcasting Co.,* 43 F. Supp. 137 (N. D. Tex., 1942); *Restatement of the Law of Contracts,* §§ 288, 458; 6 Williston, *Contracts* § 1938 (Rev. Ed. 1938).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

CHARLES FAHY,
Solicitor General.

JOHN F. DAVIS,
Solicitor, Securities and Exchange Commission.

MARCH, 1943.

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